Comments on the Restoring Internet Freedom Notice of Proposed Rulemaking

July 2017

Thomas Lenard and Scott Wallsten

409 12th Street SW ● Suite 700 ● Washington, DC 20024
Tel: (202) 828-4405 ● Email: info@techpolicyinstitute.org ● www.techpolicyinstitute.org

Comments on the *Restoring Internet Freedom Notice of Proposed Rulemaking*

Thomas Lenard and Scott Wallsten

July 17, 2017

On May 23, 2017, the Federal Communications Commission released the *Restoring Internet Freedom Notice of Proposed Rulemaking* (NPRM), aimed at reversing many of the provisions of the Open Internet Order the Commission adopted in February 2015 (2015 OIO) and returning to the "light-touch" regulatory regime that existed previously. The NPRM asks for comments on a range of legal and economic questions associated with the rulemaking. We leave the legal questions to lawyers and focus solely on economic issues.

While the NPRM asks specific questions, which we address, the fundamental question is whether BIAS providers should be covered by the rules that applied before or after the 2015 OIO. Specifically, is society likely to be better off with BIAS providers regulated under Title I or Title II of the Telecommunications Act. Similarly, is society better off with or without the "bright line" rules against blocking, throttling, and paid prioritization established in the 2015 OIO.

Economic analysis and U.S. history with Title II-style, common carrier, regulation strongly suggest that the 2015 OIO will be detrimental to innovation and to the development of both infrastructure and edge investment.

Our comments first discuss the relevant features of the 2015 OIO and incorrect or incomplete logic used to justify it. Next, it focuses on specific aspects of the Order that the NPRM would repeal, explaining the implications and why we believe their repeal would be beneficial. We also discuss the proposed cost-benefit analysis, noting that while we believe it will demonstrate that passing the NPRM will yield net benefits, it must be conducted in a neutral and rigorous fashion so that the analysis, not a desire for a particular policy outcome, drive the conclusion.

The 2015 Open Internet Order

The FCC under Chairman Tom Wheeler argued that the 2015 OIO was necessary to protect an "open Internet," which it did not define.[1] In the name of protecting this undefined good, the 2015 OIO made several changes to the long-standing rules that had covered the Internet ecosystem. In particular, it:

- Reclassified broadband Internet access service (BIAS) providers as telecommunications service providers covered by Title II of the Communications Act. Under Title II, broadband is considered a common carrier potentially subject to the full range of public-utility regulations, including regulation of rates and quality of service.
- Gave the Commission broad discretion to act against behavior it considered discriminatory under the authority provided (at least partly) by the Title II classification.
- Created "bright-line" rules against blocking, throttling and paid prioritization.

[1] Federal Communications Commission, "In the Matter of Protecting and Promoting the Open Internet," Report and Order on Remand, Declaratory Ruling, and Order, (February 6, 2015), https://apps.fcc.gov/edocs_public/attachmatch/FCC-15-24A1.pdf.

- Required enhanced transparency, mandating public disclosure of network management and commercial practices.

To some extent, the disagreement over the need for rules is based on philosophical differences regarding the role of regulation. On one side are people who believe in the "precautionary principle," in which regulations are necessary to prevent potential harms. On the other side are people who believe regulations should be promulgated to address specific problems or market failures. The 2015 OIO, however, fails to meet the criteria for either side: it does not make a coherent argument why the rules are necessary to prevent problems in theory or that they are necessary to deal with a problem observed in practice.

The Order Did Not Address a Significant Problem in Theory

The broadest issue the OIO claimed to address was Internet innovation. These rules, the Order argued, would help drive "a 'virtuous cycle' in which innovations at the edges of the network enhance consumer demand, leading to expanded investments in broadband infrastructure that, in turn, spark new innovations at the edge."[2]

The Commission claimed to be concerned about investment in Internet infrastructure and content, but appeared to worry primarily that BIAS providers could harm edge investment:

> The key insight of the virtuous cycle is that broadband providers have both the incentive and the ability to act as gatekeepers standing between edge providers and consumers. As gatekeepers, they can block access altogether; they can target competitors, including competitors to their own video services; and they can extract unfair tolls. Such conduct would, as the Commission concluded in 2010, 'reduce the rate of innovation at the edge and, in turn, the likely rate of improvements to network infrastructure.' In other words, when a broadband provider acts as a gatekeeper, it actually chokes consumer demand for the very broadband product it can supply. [3]

However, this reasoning is incomplete and, therefore, does not properly describe the various incentives. The Commission ignored two other factors that can affect both incentives to discriminate and the virtuous cycle.

First, the Order stated that BIAS providers would have an incentive to block anticompetitively, but never explained why it believed that to be true. In reality, it is not necessarily the case that a BIAS provider has an incentive to block, even when it has a competing service. As the 2015 OIO itself explained, "when a broadband provider acts as a gatekeeper, it actually chokes consumer demand for the very broadband product it can supply."[4] Simply put, blocking content that consumers want reduces the value of the broadband platform.

Even when broadband providers compete with content providers they will not necessarily have a net incentive to discriminate. It is common across many industries for distributors to sell their

[2] Ibid., para. 7.
[3] Ibid., para. 20.
[4] Ibid.

own products and services along with those of others. Supermarkets are an obvious example. Safeway does not make it hard for shoppers to buy Oreos in order to promote its own store-brand substitute, Tuxedos. In general, distributors will not find it in their interest to block their customers from accessing goods and services they find valuable.

The nature of the market can affect these incentives. Set aside, for the moment, the debate over how best to characterize competition in broadband provision, including the degree to which different services, speeds, and technologies compete with each other, and assume that ISPs have market power. Even if one accepts that premise, concerns about anticompetitive use of the gatekeeper role are largely misplaced. As Farrell and Weiser argue, "even a monopolist has incentives to provide access to its platform when it is efficient to do so, and to deny such access only when access is inefficient."[5] An efficiently functioning applications market increases the value of the platform—in this case the broadband provider—even if the provider is a monopolist:

> the platform monopolist cannot increase its overall profit by monopolizing the applications market, because it could always have charged consumers a higher platform price in the first place; it has no incentive to take profits or inefficiently hamper or exclude rivals in the applications market because it can appropriate the benefits of cheap and attractive applications in its pricing of the platform. To the contrary,… a platform monopolist has an incentive to innovate and push for improvements in its system, including better applications—in order to profit from a more valuable platform.[6]

Farrell and Weiser describe some exceptions to this general rule. Ironically, in the context of Title II regulation, an important exception can occur when the platform is subject to price regulation.[7] Price regulation might, by limiting profits in the provider's primary market, provide an incentive to leverage any market power into complementary markets when otherwise it would be inefficient to do so. In other words, regulation allowed by Title II could create precisely the type of problem the OIO purports to address.

Second, former FCC Chief Economist Tim Brennan raised the possibility that completely eliminating the ability to discriminate against different types of traffic could interrupt the virtuous circle in a different way.[8] In particular, he notes that if a BIAS provider knows a particular network investment will allow another firm to enter the market quickly and displace one of its own services it may delay that investment.

We are not, however, arguing that the Commission's concerns are completely without merit. It is conceivable that in some cases a BIAS provider may behave in a way that anticompetitively prioritizes its own products. The potential for such behavior is not limited to BIAS providers or to the Internet. It is a potential concern across the economy, which is why we have antitrust rules and agencies to enforce them. The Commission made no argument explaining why this industry

---

[5] Joseph Farrell and Phil Weiser, "Modularity, Vertical Integration, and Open Access Policies: Towards a Convergence of Antitrust and Regulation in the Internet Age," *Harvard Journal of Law and Technology* 17, no. 1 (Fall 2003): 89, doi:10.2139/ssrn.452220.
[6] Ibid., 103.
[7] This is known as Baxter's Law, see Ibid., 89.
[8] Timothy Brennan, "The Post-Internet Order Broadband Sector: Lessons from the Pre-Open Internet Order Experience," *Review of Industrial Organization* 50, no. 4 (June 2017): 469–86, doi:10.1007/s11151-016-9551-y.

requires its own set of competition rules. We discuss in more detail below why we believe antitrust is the more appropriate remedy to these concerns.

The Order Did Not Address a Significant Problem in Practice

While the Commission produced a flawed theory to justify the rules, it also produced little evidence that the Order addressed an actual problem. The existence of harms in the marketplace is a necessary condition for the 2015 OIO to yield benefits. In the absence of such harms, the OIO can't produce benefits since benefits by definition are the reduction in harms.

As former FCC Chief Economist Timothy Brennan has noted, "The record of alleged (rather than theoretical) conduct that the FCC cited in support of [the 2015 OIO] is meager."[9] The NPRM for the 2015 OIO referred to two well-publicized cases that had occurred well before 2015, indeed even before the original *2010 Open Internet Order* was adopted:[10]

- Madison River, a small North Carolina telephone company, was found to be blocking Vonage VoIP in 2005.
- Comcast engaged in network management practices to avoid congestion in 2007—deferring BitTorrent traffic to off-peak times—that were criticized for lack of transparency.

Both of these problems were remedied relatively quickly and easily in the absence of any Open Internet Order. Moreover, it is questionable whether either of these practices harmed consumers. Madison River's practice might have been necessary to make its own service economically viable. According to Brennan,

> If Madison River realized that offering DSL would mean giving up profits from its standard voice service and that the FCC would block its only means for recovering those profits, it may not have offered DSL at all, at least as early as 2005…. [This episode] suggest[s] that OI 2015 enforcement could discourage new business models by BIAS providers if they worry that the FCC would then force them to forgo profits from prior services.[11]

The Comcast practice was aimed at reducing congestion—a benefit for many users—and affected a file-sharing service primarily used to transfer pirated works. As Brennan noted, "The FCC's action with regard to BitTorrent challenges the ability of BIAS providers to manage congestion on their networks."[12]

Subsequent to the 2010 Order, the Commission found two examples "related to the open Internet rules and norms," both in 2012.[13] The first involved a refusal by Verizon to allow tethering apps

[9] Ibid., 470.
[10] The 2015 OIO replaced the 2010 Order, which was vacated by the U.S. Court of Appeals for the DC Circuit.
[11] Brennan, "The Post-Internet Order Broadband Sector," 476.
[12] Ibid., 477.
[13] Thomas Lenard, "Comments Filed with the Federal Communications Commission on 'Protecting and Promoting the Open Internet' | The Technology Policy Institute," accessed July 14, 2017, https://techpolicyinstitute.org/testimony_filing/comments-filed-with-the-federal-communications-commission-on-protecting-and-promoting-the-open-internet/.

on Verizon smartphones. The second was consumer complaints concerning AT&T's refusal to permit Apple's FaceTime application to use its mobile network, restricting its use to times the user was connected with Wi-Fi and, subsequently, to users willing to pay for data usage above a cap. It is unclear whether either of these actions, which involved highly bandwidth-intensive apps, was harmful to consumers. Both involved managing applications that potentially used substantial capacity that if unrestricted might have imposed costs on other consumers.

It is also unclear whether either of these cases violated the open Internet rules. The Verizon case, settled for $1.25 million, was related to the openness requirements attached to Verizon's Upper C-Block license. With respect to the AT&T case, "the Commission did not conclude whether such a practice violated our open Internet principles."

In the remainder of this report we discuss the issues underlying the tension between 2015 OIO and the current NPRM.

2017 Restoring Internet Freedom NPRM (NPRM)

The 2017 NPRM proposes to end the public utility treatment of broadband providers by restoring the information service (Title I) classification of BIAS and restoring the private mobile service classification of mobile broadband Internet access service. The NPRM also proposes to rescind the general conduct standard. Beyond that, the Commission is asking for comment on whether it should retain any of the bright-line rules and/or the enhanced transparency rule. We discuss these issues in this section.

Title II Classification

Probably the most far-reaching aspect of the 2015 OIO was reclassifying BIAS providers as Title II telecommunications service providers, thereby giving the FCC authority for public utility-style regulation of broadband markets. Public utility regulation generally entails some form of non-discriminatory open access requirement and price regulation. The problem with Title II classification is that it gives the FCC broad authority to regulate prices and quality of service.

It is true that the FCC chose to avoid regulating retail prices for now. However, it is not possible to bind a future Commission's hands on the issue. After all, the second sentence of Title II says "All charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable, and any such charge, practice, classification, or regulation that is unjust or unreasonable is hereby declared to be unlawful."[14] In other words, the Commission would have wide leeway in deciding if any aspect of an ISPs business is "just and reasonable."

The U.S. has a long, troubled, history with common carrier regulation such as this. As Wallsten noted in an earlier essay,

[14] https://transition.fcc.gov/Reports/1934new.pdf

> Even when established with the best of intentions, however, regulations do not necessarily work for the public good. Instead, they become the product of lobbying by interested parties ranging from companies to public interest groups to Congress and others over how to distribute profits. The interactions between the regulator and those parties inevitably lead to increasingly complex and politicized regulatory regimes.[15]

That is what we observed with rail, trucking, and gas, which were all subject to common carrier regulation. Wallsten continued:

> Start with the Interstate Commerce Commission (ICC), which was established in 1887 to regulate railroads in response to farmers' claims of rate discrimination and decommissioned at the end of 1995. Net neutrality proponents would have swooned over the ICC's enabling legislation, which made it illegal for any common carrier to "make or give any undue or unreasonable preference or advantage to any particular person, company, firm, corporation, or locality, or any particular description of traffic, in any respect whatsoever…" In other words, no preferential treatment.
>
> Like net neutrality, that nondiscrimination sounds simple, but it wasn't. In 1908, railroads filed nearly 229,000 rates at the ICC. These tariffs differed by distance and what was being transported. The ICC even had a full-time "classification committee" dedicated to setting allowable maximum prices for different types of freight.
>
> The result? Initially, railroad profits increased. When trucking began to compete with railroads, the ICC regulated trucks, too. That was great for the trucking industry, which became a legal cartel with no incentive to innovate and later fought tooth and nail against deregulation. Meanwhile, regulations prevented railroad companies from adapting, driving several into bankruptcy.
>
> The ICC's experience was hardly unique. Consider natural gas. Even though one cubic meter of gas is pretty much like any other cubic meter of gas, in 1976 the energy regulator established five types of gas based on vintage in order to promote exploration. By the time this regulatory regime was dismantled in 1978, the number of categories had ballooned to 28.[16]

There is no reason to believe that the outcomes described above would be different in the case of broadband provision. Indeed, we already saw the beginnings of such lobbying, including complaints against tiny MetroPCS for its streaming service, disagreements between Comcast and Netflix, and hand-wringing over so-called zero-rating.

The 2015 OIO also argued that the presence of a so-called "terminating access" monopoly justified Title II classification. That is, the Commission noted, "regardless of the competition in the local market for broadband Internet access, once a consumer chooses a broadband provider, that provider has a monopoly on access to the subscriber."[17] The Commission was concerned that

---

[15] Thomas Lenard, "Comments Filed with the Federal Communications Commission on 'Protecting and Promoting the Open Internet' | The Technology Policy Institute," accessed July 14, 2017, https://techpolicyinstitute.org/testimony_filing/comments-filed-with-the-federal-communications-commission-on-protecting-and-promoting-the-open-internet/.

[16] Ibid.

[17] Federal Communications Commission, "In the Matter of Protecting and Promoting the Open Internet," para. 80.

"The broadband provider's position as gatekeeper is strengthened by the high switching costs consumers face when seeking a new service."

Switching broadband providers entails costs, to be sure. However, the implication that switching costs render competition meaningless is inconsistent with the substantial sums on marketing and incentives to induce subscribers to remain and competitors' subscribers to switch service. Broadband providers have a strong incentive to make sure their subscribers can get the content they want. Otherwise, they will lose subscribers and fail to attract new ones. Even if only a small percentage of subscribers are willing to incur switching costs, providers will be constrained from the types of anticompetitive activities about which the Commission is concerned.

Bright-Line Rules

The 2015 OIO determined that certain types of behavior should not be allowed at all. It called these prohibitions "bright line" rules. The OIO, however, did not establish that the prohibited behavior is necessarily bad and failed to recognize that it may often benefit consumers.

The three bright-line rules are:[18]

> ***No Blocking****….A person engaged in the provision of broadband Internet access service, insofar as such person is so engaged, shall not block lawful content, applications, services, or non-harmful devices, subject to reasonable network management.*
>
> ***No Throttling****….A person engaged in the provision of broadband Internet access service, insofar as such person is so engaged, shall not impair or degrade lawful Internet traffic on the basis of Internet content, application, or service, or use of non-harmful device, subject to reasonable network management.*
>
> ***No Paid Prioritization****….A person engaged in the provision of broadband Internet access service, insofar as such person is so engaged, shall not engage in paid prioritization. "Paid prioritization" refers to the management of a broadband provider's network to directly or indirectly favor some traffic over other traffic, including through use of techniques such as traffic shaping, prioritization, resource reservation, or other forms of preferential traffic management, either (a) in exchange for consideration (monetary or otherwise) from a third party, or (b) to benefit an affiliated entity.* [Italics in original, bold emphasis added.]

Together, the rules set the price of best-effort service to content providers at zero.[19] The prohibition on paid prioritization precludes BIAS providers from charging content providers different prices for different levels of service.

As Michael Katz has written,[20] the Commission's ban on charging edge providers has at least three problems:

---

[18] Ibid., paras. 15, 16, 18.
[19] Brennan, "The Post-Internet Order Broadband Sector," 474; Michael L. Katz, "Wither U.S. Net Neutrality Regulation?," *Review of Industrial Organization* 50, no. 4 (June 1, 2017): 443, doi:10.1007/s11151-017-9573-0.,
[20] Katz, "Wither U.S. Net Neutrality Regulation?," 448–49.

> First, it is well-established in the two-sided pricing literature that charging non-zero prices to users on both sides of the platform is typically efficient. Hence, even when the terminating access problem would otherwise lead to inefficiently high prices to edge providers, reducing those prices to zero may be inefficient.
>
> Second, and closely related, there is a 'waterboard effect:' Forcing BIAS providers to charge lower prices to edge providers creates incentives for BIAS providers to charge higher prices to end users. This effect arises because end users are less valuable to a BIAS provider if they cannot be used as a means of deriving revenue from edge providers.
>
> A third problem with the Commission's blanket ban is that many important applications have a mechanism for eliminating the terminating access problem. Several of the largest edge providers of video and music streaming services, as well as most e-commerce sites that sell physical products, charge end users fees for their services. When those fees can vary with the end user's choice of BIAS provider, edge providers have a means of overcoming the terminating access problem.

Brennan also observes that "A predictable consequence of that regulation (i.e., regulating prices to content providers) is higher prices on the other side of the market—end user payments for broadband service—than what would have occurred in its absence."[21]

In this context, Connolly et al specifically address the effects of OIO rules on the Digital Divide, a significant problem as indicated by the 2015 Pew estimate that 21 percent of U.S. households do not have Internet.[22] They also observe that "Since the OIO prevents ISPs from charging any fees to content providers, it will affect the last mile fees that ISPs charge end-users."[23] In the absence of regulation, "ISPs could charge CSPs [Content Service Providers] higher prices in order to lower the last-mile fees for consumers in an attempt to maximize their end-user subscriptions."[24] Thus, she argues, the OIO is likely to widen rather than help close the digital divide.

The bright-line rules imply a cross subsidization that goes in the wrong direction, from light users of broadband capacity to heavy users. As Hylton observes, "Some broadband-intensive providers of internet content, such as Netflix, would—in the absence of differential pricing—impose extraordinary congestion costs that would result in an internal subsidy from consumers of other internet services. Hence, permitting the network owner to price differentially can and probably would enhance consumer welfare.[25] Since consumers of Netflix and similar services are on average wealthier than the average U.S. consumer, Hylton concludes that "the net neutrality norm at present offers an unambiguous reduction in distributional efficiency that is coupled with a likely negative impact on general efficiency."[26]

---

[21] Brennan, "The Post-Internet Order Broadband Sector.", p. 475
[22] Michelle Connolly, Clement Lee, and Renhao Tan, "The Digital Divide and Other Economic Considerations for Network Neutrality," *Review of Industrial Organization* 50, no. 4 (June 1, 2017): 537–54, doi:10.1007/s11151-016-9554-8., 538
[23] Ibid., 541
[24] Ibid., 542
[25] Keith N. Hylton, "Law, Social Welfare, and Net Neutrality," *Review of Industrial Organization* 50, no. 4 (June 1, 2017): 417–29, doi:10.1007/s11151-016-9552-x. p. 420
[26] Ibid., 423.

Proponents of the ban on paid prioritization believe it helps smaller companies and new entrants compete against big companies like Google and Facebook who presumably can more easily afford to pay for priority access to ISP customers. Katz suggests the same logic would preclude some firms from purchasing more electricity than others so they do not obtain a competitive advantage or preclude e-commerce firms from purchasing faster delivery from FedEX or UPS or offering free shipping. He also notes that entrants and smaller firms should not necessarily be at a disadvantage if the access charges they face vary with traffic volume. He observes that "A ban on paid prioritization is similar to a cartel agreement that bans competition along certain dimensions."[27] It focuses on competitor welfare rather than consumer welfare and efficiency.

Katz finds that "banning paid priority eliminates entry and has exactly the opposite of the effect that is claimed by its proponents."[28] He argues that paid prioritization "can facilitate entry … [if] there are conditions under which the choice of a different termination quality than that of the incumbent allows the entrant to differentiate its product and, thus, relax price competition that would otherwise be so intense that the entrant could not cover its fixed costs."[29]

Katz concludes that "This discussion of paid prioritization does not provide definitive conclusions with regard to its welfare effects. But it does establish that there is not a sound theoretical argument for the assertion that paid prioritization generally harms welfare or suppresses entry. Rather, the effects of paid prioritization are fact specific."[30] This again suggests that an antitrust investigation is the appropriate forum if there is reason to believe that competition or consumers are being harmed.

More generally, even if a particular set of bright-line rules seem right at a given moment in time, they may not be the next moment. It is for this reason that courts have been generally skeptical about the validity of per-se illegal behavior and why it is so difficult to prove such behavior in antitrust cases.

General Conduct Standard (GCS)

The Commission expressed concern that the bright lines may be insufficient to stop all behavior it deemed inappropriate and so included a "catch-all standard," also known as the General Conduct Standard.[31] It reads as follows:

> *Any person engaged in the provision of broadband Internet access service…shall not unreasonably interfere with or unreasonably disadvantage (i) end users' ability to select, access, and use broadband Internet access service or the lawful Internet content, applications, services, or devices of their choice, or (ii) edge providers' ability to make lawful content, applications, services, or devices available to end users. Reasonable network management shall not be considered a violation of this rule.* [Italics in original].

[27] Katz, "Wither U.S. Net Neutrality Regulation?", 454
[28] Ibid., 457
[29] Ibid., 456
[30] Ibid., 458
[31] Federal Communications Commission, "In the Matter of Protecting and Promoting the Open Internet," para. 21.

A major problem with the GCS is its vagueness. The Commission has not explained how it would be applied and what business models would be allowed. The existence of this provision is likely to lead to a steady stream of complaints from interested parties and continual second-guessing of providers' business practices and pricing decisions on the part of the Commission itself. Putting broadband providers in the position of constantly having to justify their business practices as "reasonable" goes a long way toward establishing a *de facto* utility-type regulatory regime, with its attendant problems—reduced incentives to innovate, invest and provide services consumers want—even in the absence of Title II reclassification.

This type of provision is a prime illustration of the superiority of the antitrust approach, which we discuss below. Enforcement against "unreasonable" discrimination, which seems to be the motivation behind the GCS, should be based on competition law principles drawn from economics and antitrust law.

2015 OIO Enhanced Transparency Requirement

The OIO added additional transparency requirements to those that already put in place by the 2010 Order. Transparency is important—consumers need to know what they are purchasing in order to make informed decisions and to ensure that markets works properly. When thinking about what information ISPs are required to disclose, however, the Commission should be cognizant that certain types of required disclosure can have unintended consequences.

In particular, as a 2001 OECD report observed, "The competitive risks of increased price transparency, under certain market conditions, have not always been sufficiently appreciated by government policy makers. There have been instances where government mandated increases in price transparency seemed to have produced higher rather than lower prices, probably because they facilitated anti-competitive coordination among sellers."[32] The OECD analysis indicates that the competitive risks of increased price transparency are greater in markets characterized by high levels of concentration, a small number of sellers, and high barriers to entry.[33]

The issue is that price disclosure requirements may make it more difficult for customers on either side of the two-sided broadband platform to negotiate price discounts, because providers may be reluctant to offer discounts that must be made public to everyone.

The economics literature also makes clear that mandated price disclosure may facilitate cartel behavior: "The more prices exceed competitive levels, the more individual sellers stand to gain, at least in the short run, by secretly cutting price. This is the 'prisoner's dilemma' which tends to undermine all attempts at oligopolistic co-ordination, whether formal (i.e., explicit collusion) or otherwise (i.e., tacit collusion, conscious parallelism, price leadership etc.). Stable anti-competitive co-ordination requires that firms find a way to make co-operation the 'dominant strategy', meaning a credible way must be found to detect and punish cheating.[34] Providing

[32] Committee on Competition Law and Policy, "Policy Roundtable: Price Transparency" (Organization for Economic Co-operation and Development, September 11, 2001), http://www.oecd.org/competition/abuse/2535975.pdf., p. 9
[33] Ibid., 10, 25
[34] Ibid., 24

transparency to a concentrated market aids in the detection of cheaters, thereby allowing the stable anti-competitive equilibrium to develop. The OECD report cites empirical studies of the National Industrial Recovery Act (NIRA) and the rail sector where government-mandated price transparency facilitated collusion and higher prices.[35]

In short, transparency is important, but the Commission should take care to consider when mandatory disclosure might paradoxically lead to higher prices for consumers.

Privacy

A major benefit of the reclassification of BIAS as a Title I service is returning privacy enforcement responsibilities over broadband providers to the Federal Trade Commission, which lost that responsibility when the FCC classified broadband providers as Title II common carriers. Common carriers are exempt from FTC jurisdiction.

The FTC has long been the principal U.S. privacy enforcement agency and, overall, has done a good job. The FCC, on the other hand, has limited expertise in this area. This was demonstrated by the privacy rule the agency adopted with its new authority subsequent to adoption of the 2015 OIO. The FCC privacy rule did not reflect an appreciation of the benefits that flow from information collection and use and the costs associated with limiting that flow.[36] Recent action by congress under the Congressional Review Act repealed the FCC's privacy rule, but the common carrier designation of broadband providers needs to be rescinded to return jurisdiction to the FTC.

The Antitrust Alternative

One implication of the NPRM and, as discussed below, part of the relevant comparison for a cost-benefit analysis, is that BIAS behavior will once again be largely governed by antitrust laws. Economists have generally been favorable toward using the antitrust laws, which rely on a case-by-case approach, to address net neutrality issues.[37] Though antitrust is not without its problems, it rests on a fairly well defined set of pro-consumer, economic efficiency principles and goals, which gives antitrust enforcement some predictability.

The practices proscribed by the 2015 OIO—e.g., charging a non-zero price to edge providers and charging more for higher quality service—are usually, but not always, procompetitive. Antitrust is preferable to the OIO rules, because antitrust can be applied on a case-by-case basis when the facts indicate that the conduct is anticompetitive. As Hylton wrote, "Antitrust laws already exist for regulating anticompetitive conduct, and they attempt to regulate with a finer brush than the net neutrality rule."[38] He concludes, "For every potential social gain that might be provided by

---

[35] Ibid., 32-33

[36] "An Economic Analysis of the FCC's Privacy Notice of Proposed Rulemaking | The Technology Policy Institute," accessed July 14, 2017, https://techpolicyinstitute.org/testimony_filing/an-economic-analysis-of-the-fccs-privacy-notice-of-proposed-rulemaking/.

[37] William J. Baumol et al., "Economists' Statement on Network Neutrality Policy," SSRN Scholarly Paper (Rochester, NY: Social Science Research Network, March 1, 2007), https://papers.ssrn.com/abstract=976889.

[38] Hylton, "Law, Social Welfare, and Net Neutrality.", p. 424

the neutrality policy, an alternative, narrower policy exists that would be at least as effective and less likely to have harmful side effects."[39]

Ohlhausen writes that "net neutrality proponents underestimate the ability of market forces, combined with antitrust oversight, to shield consumers from harmful ISP content discrimination."[40] She provides examples of the superiority of a rule-of-reason approach relative to the *per se* approach reflected in the OIO rules:

> Suppose that a broadband ISP with market power decided to contract with an edge provider to exclude all competing content from its last mile network. Pursuant to the agreement, the ISP blocks or materially degrades competing content offered by other edge providers. As a result, the conspiring edge provider's market share and power increase vis-à-vis its rivals, while the ISP's consumers lose preferred content. The vertical boycott would likely fail scrutiny under the rule of reason unless the ISP and edge provider could proffer sufficient procompetitive justifications.[41]

> Imagine that an edge provider offers bandwidth-heavy content for which there is great consumer demand versus alternative content. To maximize the value of its content, the edge provider partners with an ISP that agrees to prioritize its content over lesser alternatives. Is there an antitrust violation? There may not be, especially if the parties can show that the procompetitive effects of the restraint—faster delivery of content favored by consumers—outweighed the exclusionary effects. The rule of reason adopts an all-encompassing inquiry, paying close attention to the consumer benefits and downsides of the challenged practice based on the facts at hand. If that inquiry shows that a particular act of paid prioritization, throttling, or blocking enhanced consumer welfare, then that should be the end of the matter from a competition standpoint.[42]

Antitrust laws have been proven robust across nearly every industry and are crucial to maintaining a vibrant, competitive economy. There is no reason they should not also apply in this case.

Cost-Benefit Analysis (CBA)

The NPRM stresses the importance of economic analysis and states that the Commission will conduct its own CBA of the major elements of its proposal.[43] The Commission seeks comment on how to conduct its CBA and indicates it will follow Office of Management and Budget Circular A-4, which provides guidance for performing regulatory analysis required for executive branch agency regulations by Executive Order 12866.

A regulatory analysis following these guidelines begins by addressing two issues.

---

[39] Ibid., 429
[40] Maureen Ohlhausen, "Antitrust Over Net Neutrality: Why We Should Take Competition in Broadband Seriously," *Colorado Technology Law Journal*, The Digital Broadband Migration: The Evolving Industry Structure of the Digital Broadband Landscape, 15, no. 1 (December 25, 2016): 119–49.
[41] Ibid., 142
[42] Ibid., 142
[43] Federal Communications Commission, "In the Matter of Restoring Internet Freedom," May 23, 2017, paras. 105, 107, https://apps.fcc.gov/edocs_public/attachmatch/FCC-17-60A1.pdf.

First, it must specify the problem the regulation is intended to address—in the words of Circular A-4 "explain whether the action is intended to address a significant market failure or to meet some other compelling public need…"[44] Second, and relatedly, it must specify the baseline for analysis. That is, to what is the analysis comparing the costs and benefits of the regulation?

In this case, the analysis is the one that should have been done prior to the 2015 OIO, only in this case the status quo is the rule and the proposal is, essentially, repealing the rule. The world without the OIO is one in which the FTC is responsible for privacy enforcement and antitrust rules govern firm behavior. Thus, the benefits and costs of rescinding the 2015 regulation will largely mirror the costs and benefits of adopting it.

As we discussed, the purported benefits of the 2015 OIO are largely speculative and hypothetical while the costs are more concrete. We expect the net benefits of adopting the NPRM and repealing the 2015 OIO to be positive. Nevertheless, the cost-benefit analysis must be done in a neutral fashion, use best-practice cost-benefit tools, follow guidelines established by the OMB, and be conducted so that the analysis, not a desire for a particular policy outcome, drive the conclusion.

Conclusion

The 2015 OIO was passed with little to no economic analysis or review of historical precedent. It created a regime in which broadband service is treated as a common carrier. Common carrier rules, however, have proven time and again to be costly to the economy, consumers, and innovation. They create a situation in which it makes more sense for competitors to lobby the regulator than to compete on the basis of prices or innovation. It was already possible to see this costly behavior taking place, with regulatory complaints about a tiny wireless company offering unlimited video streaming, popular zero-rating practices, and commercial interactions between large companies.

Returning Internet rules to those that yielded so much success prior to 2015 is sensible and will prevent us from falling into a regulatory morass of the type that crippled other network industries like rail and trucking for decades. Competition governed by true antitrust oversight is the right way forward.

[44] Office of Management and Budget, "Circular A-4" (Office of Management and Budget, September 17, 2003), https://obamawhitehouse.archives.gov/omb/circulars_a004_a-4/.